

Internal Revenue Service
Tax Exempt and Government Entities Division
Exempt Organizations: Examinations

Department of the Treasury

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Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

9/30/20XX, 9/30/20XX and

9/30/20XX

Person to Contact/ID Number:

**CERTIFIED MAIL – RETURN RECEIPT
REQUESTED**

Contact Numbers:

Telephone:

Fax:

Dear :

In a determination letter dated September, 19XX, you were held to be exempt from Federal income tax under section 501(c)(7) of the Internal Revenue Code (the Code). Based on recent information received, we have determined you have not operated in accordance with the provisions of section 501(c)(7) of the Code. According your exemption from Federal income tax is revoked effective October 1, 20XX. This is a final letter with regard to your exempt status.

We previously provided you a report of examination explaining why we believe revocation of your exempt status was necessary. At that time, we informed you of your right to contact the Taxpayer Advocate, as well as your appeal rights. On June 4, 20XX you signed Form 6018-A, *Consent to Proposed Action*, agreeing to the revocation of your exempt status under section 501(c)(7) of the Code. You are required to file Federal income tax returns for the tax period(s) shown above. If you have not yet filed these returns, please file them with the Ogden Service Center within 60 days from the date of this letter, unless a request for extension is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Internal Revenue Service
Tax Exempt and Government Entities Division
Exempt Organizations: Examinations

Department of the Treasury

Date: April 9, 2012

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

9/30/20XX and 9/30/20XX

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail – Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter revoking your exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s)

shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Internal Revenue Service
Office of the Taxpayer Advocate

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018
Report of Examination
Envelope

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS		Schedule number or exhibit
Name of taxpayer	Tax Identification Number		Year/Period ended 20XX, 20XX

Issues:

Whether the tax-exempt status of a 501(c)(7) organization that sponsors competitions, with income from non-members and non-exempt operations in excess of 15% of total revenue, continues to qualify for exemption or is subject to revocation of its exempt status.

Facts:

The is an organization exempt under Section 501(c)(7) of the Internal Revenue Code. The organization's mission, as stated on the Form 990 filed for the year ended September 30, 20XX, is to hold five tournament competition during the year. The organization's membership consists of clubs operating within the State of who pay dues of \$.00 per year. The organization sponsors either four or five competitions each year, in alternating years. These member clubs are affiliated with the . The is also an affiliated club with the . There are no individual members in the

The four or five tournament competition held each year are open to individual members of the . The total number of days the club is operating during any given year is between 21 and 27, as the club is only open during the days of the four or five competitions held annually. The participants are not limited to the members of the member clubs of the . The taxpayer provided the examiner with a schedule of revenue from sources inside and outside the State of . The data from this schedule is summarized below:

<u>Year Ended 9/30/20XX</u>	<u>Total</u>	<u>Sourced</u>	<u>Non- Sourced</u>
Revenue	\$	\$ %	\$ %

These amounts are shown net of the prize payouts of \$. The organization does not have sufficient information to calculate the revenue before payouts broken down between and non- sources. The Service has allocated the prize payouts using the same ratio as that of the and non- income to total income (above) to arrive at gross revenue income. In addition to the revenue, the organization receives revenue from numerous other sources including kitchen revenue, practice revenue, pre-squad, re-squad and shell revenue, and soda machine sales. No records are maintained to identify whether this revenue is earned from participants from within or outside of the State of . During the year ended September 30, 20XX the organization received "Lead Reclamation" revenue, as the result of the sale of lead on the grounds from the various competitions. It was indicated that approximately every 10 years, lead is gathered up by an independent entity that pays the organization based on the amount collected. Other sources of revenue from activities unrelated to the exempt purpose of the organization include the rental of campsites to participants in the competitions; advertising in the program provided to

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participants in all the annual competitions; revenue collected from vendors who rent spots to sell there wares to tournament participants, providing ammunition and similar products and providing repair services for participants. A summary of the receipts follows:

9/30/XX:

<u>Source</u>	<u>Total</u>	<u>Member</u>	<u>Non-Member</u>	<u>Non-Traditional/ Non-Exempt</u>
Membership Dues	\$ 0	\$ 0		
Revenue	0	0	\$ 0	
Rebate	0			\$0
300	0	0	0	
Zone	0		0	
Investment Income	0			0
Campsite Rentals	0			0
Program Ad Sales	0			0
Soda Machine	0			0
Vendor 20XX	0			0
Memorial	0		0	
AT&T Profit Share	0			0
Insurance Refund	0			0
Lead Reclamation	0			0
Misc	0			0
Total	\$			

The sources of income identified above as Revenue", " 300" and " Zone represent revenue from various competitions and are allocated accordingly between member and non-member income using the percentage described above.

The items included as non-exempt revenue are included in that category either as the result of being non-traditional income for a social club exempt under Section 501(c)(7) of the IRC or because no records were kept to identify whether the source of the income was from member or non-member sources.

The amount of the payouts which were netted against the total receipts were not identified as to whether the revenue that generated the amount of the payouts was from or non- sources. Because the organization did not maintain records identifying the revenue as coming from member and non-member sources (from members of the member clubs vs. non-members of the member clubs), for comparative purposes, the Internal Revenue Service included all sourced shoot revenue as coming from members and all other revenue as being from non-members. The payouts were allocated between and non- based on the same ratio.

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9/30/20XX:

The taxpayer provided a schedule of revenue reporting total shoot revenues of \$, which agrees to the revenue reported on the Form 990 filed for the year ended 9/30/20XX. Also provided by the taxpayer was a schedule reporting the allocation of the revenue from event fees, allocated between participants from within and from outside of the State of . The percentages of and non- revenue as provided on this schedule were used to allocate total revenues between member and non-member (non-) sources. sourced revenue as reported by the taxpayer totaled % and non-member revenue totaled %. Total income as reported on this Form 990 is detailed below:

<u>Source</u>	<u>Total</u>	<u>Member</u>	<u>Non-Member</u>	<u>Non-Traditional/ Non-Exempt</u>
Membership Dues	\$	\$		
Revenue				
Rebate				
300				
Investment Income				
Campsite Rentals				
Program Ad Sales				
Other				
Total	\$	\$	\$	\$

The total of all the revenue for the year ended 9/30/20XX per the Form 990 is \$.

For the years ending September 30, 20XX and September 30, 20XX the non-member and non-exempt revenue is in excess of the 15% limitation.

The organization placed an advertisement in the Magazine advertising its competitions to be held during the 20XX season. The advertisement was a full page ad and included the dates of competitions to be held in June, 20XX. Included in the ad was a statement indicating \$ in prize money, information about camping and vendor information and the dates of other competitions to be held in May, July and September, 20XX. This advertisement was inspected by the examining agent and did not indicate that the competitions were limited to members of the

The Internal Revenue Service considered Internal Revenue Code Section 277 – Deductions incurred by certain membership organizations in transactions with members and concluded that no services, insurance, goods or items of value to members were provided in excess of income derived from members.

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Law:

Primary Position:

Internal Revenue Code Section 501(c)(7) applies to clubs organized for the pleasure, recreation and other non-profitable purposes, substantially all of the activities of which are for such purposes and no part of the net earnings inure to the benefit of any private shareholder.

Treasury Regulation 1.501(c)(7)-1(b) states that a club which engages in business, such as making its social and recreational facilities available to the general public or by selling real estate, timber or other products is not operated exclusively for pleasure, recreation or other non-profitable purposes. This regulation further states that solicitation by advertisement or otherwise for public patronage of its facilities is prima facie evidence that the club is engaging in business and is not being operated exclusively for pleasure, recreation or social purposes.

Public Law 94-568 provides certain limitations on non-member income and investment income social clubs may receive without jeopardizing its exempt status. P.L. 94-568 states that it is intended that social clubs may be permitted to receive up to 35% of their gross receipts, including investment income from sources outside their membership without losing their exempt status. Within this 35% amount not more than 15% of the gross receipts should be derived from the general public.

Secondary Position:

Rev. Rul. 58-589, 1958-2 C.B. 266 sets forth criteria for exemption under Section 501(c)(7) of the Code, and provides that a club must have an established membership of individuals, personal contacts and fellowship. It also provides that, while the regulations indicate that a club may lose its exemption if it makes its facilities available to the general public, this does not mean that any dealings with non-members will automatically cause a club to lose its exemption. A club may receive some income from the general public, that is, persons other than members and bona fide guests, or permit the general public to participate in its affairs, provided that such participation is incidental to and in furtherance of the club's exempt purposes, such as dealings with the general public and the receipt of income therefrom does not indicate the existence of a club purpose to make a profit, and the income does not inure to the club members.

Rev. Rul. 67-428, 1967-2 C.B. 204 holds that an organization whose membership consists entirely of artificial entities does not qualify for exemption from Federal income tax under section 501(c)(7). This Revenue Rule emphasizes that artificial entities are incapable of producing the personal contacts and fellowship contemplated by section 501(c)(7) and indicates that artificial entities, such as corporations, are not a type of "member" that is considered as falling within the term member for purposes of Section 501(c)(7) of the Internal Revenue Code.

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IRS Position:

Position 1:

It is the position of the Internal Revenue Service that the revenue collected from the Non-participants in the competitions sponsored by the organization represents non-member revenue and that the revenue from the non-traditional sources identified above represents non-exempt revenue. During the year ended September 30, 20XX this represents approximately % of the total revenue realized by the organization. For the 20XX year, this represents approximately % of the total revenue. Based on this analysis, the organization does not qualify for exemption under Section 501(c)(7) of the Internal Revenue Code.

The organization operates between 21 and 27 days per year, per information obtained during the initial interview. It does not appear, given the limited number of days that the organization is open and operating, that the organization promotes the social and recreational needs of the members. The entity appears to operate as a venue for the competitions open to members of the , regardless of their affiliation with the members of the . The membership of the organization is comprised of based clubs and not individuals. It is the position of the Internal Revenue Service that the necessary fellowship and social interaction among members is lacking given the composition of the membership, and the limited span of time that the club operates during any calendar year.

Position 2:

The organization does not qualify for exemption under Section 501(c)(7) of the Internal Revenue Code because its membership consists entirely of artificial entities and not individual members. The required personal contacts and fellowship discussed in Revenue Rule 58-589, 1958-2 C.B.266 are not found in the operations of this organization.

Taxpayer's Position:

The taxpayer is in agreement with the proposed revocation of the organization's status as a social club exempt from federal tax under Internal Revenue Code Section 501(c)(7).

Conclusion:

The Internal Revenue Service is proposing revocation of the organization's exempt status under Section 501(c)(7) of the Internal Revenue Code as of October 1, 20XX.